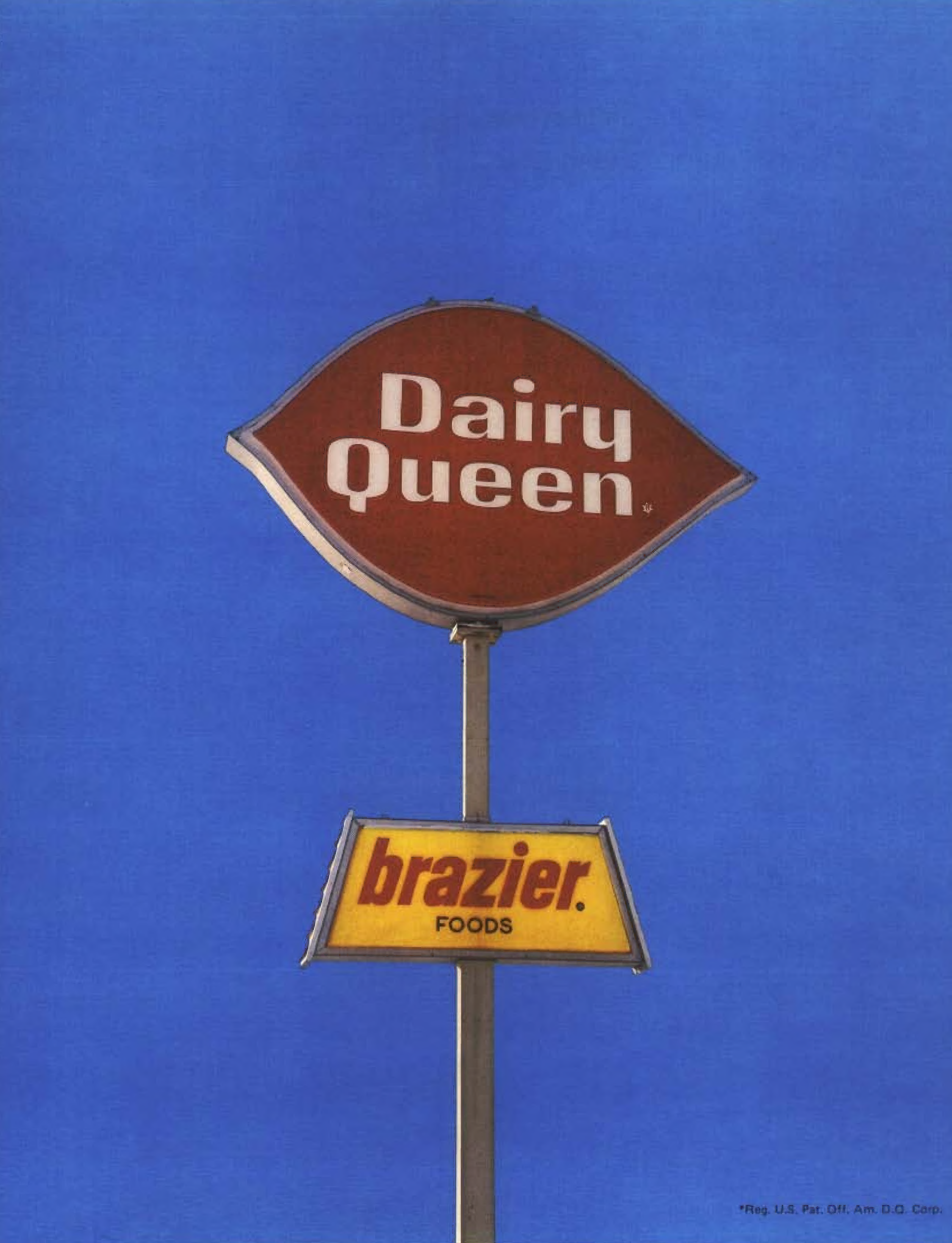
INTERNATIONAL DAIRY QUEEN, INC.

1979 Annual Report


Dairy Queen
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FINANCIAL SUMMARY

(In thousands except per share amounts)

	1979	1978	1977	1976	1975	1974	1973
OPERATIONS:							
(Fiscal year ended November 30)							
Revenues:							
Net sales:							
Food and supplies	**$40,695**	$37,870	$34,860	$30,799	$27,992	$25,907	$23,923
Equipment	**6,178**	5,862	4,549	4,050	2,986	3,953	3,046
Mix	**4,941**	5,120	4,524	4,430	4,100	4,213	3,870
Other	**2,599**	3,338	2,651	2,214	1,749	2,000	2,505
	54,413	52,190	46,584	41,493	36,827	36,073	33,344
Service fees	**13,049**	11,641	10,482	9,930	9,212	8,431	7,541
Franchise sales and other fees	**2,920**	2,739	2,418	2,430	2,926	2,716	2,374
Real estate finance and rental income	**3,357**	3,176	3,113	3,895	4,065	3,846	3,557
Other	**1,132**	1,113	835	1,188	1,471	1,575	1,714
	74,871	70,859	63,432	58,936	54,501	52,641	48,530
Costs and expenses:							
Cost of sales	**48,549**	46,989	42,242	38,286	33,729	32,524	30,188
Expenses applicable to real estate finance and rental income	**2,777**	2,747	2,673	3,373	3,564	3,470	3,328
Selling, general and administrative	**13,407**	12,672	12,661	13,078	13,337	12,742	11,899
Interest	**2,050**	1,873	1,711	1,975	2,268	2,782	2,157
	66,783	64,281	59,287	56,712	52,898	51,518	47,572
Income before income taxes	**8,088**	6,578	4,145	2,224	1,603	1,123	958
Income taxes	**3,920**	3,170	1,828	845	595	305	261
Income before cumulative effect of a change in accounting principle	**4,168**	3,408	2,317	1,379	1,008	818	697
Cumulative effect on years 1976 and prior for the change in method of accounting for leases	—	—	(346)	—	—	—	—
Net income	**$ 4,168**	$ 3,408	$ 1,971	$ 1,379	$ 1,008	$ 818	$ 697
Net income per common share before cumulative effect of a change in accounting principle	**$1.03**	$ .72	$ .42	$ .22	$ .17	$ .15	$ .12
Cumulative effect on years 1976 and prior for the change in method of accounting for leases	—	—	(.06)	—	—	—	—
Net income per common share	**$1.03**	$ .72	$ .36	$ .22	$ .17	$ .15	$ .12
Average common and common equivalent shares outstanding	**4,135**	4,853	5,583	6,361	6,393	6,389	6,292

TO OUR SHAREHOLDERS:

We are pleased to report that during fiscal 1979 your Company again realized growth in revenues and net income. Revenues increased to $74,871,082 in 1979 from $70,858,953 in 1978. Net income increased to $4,167,900 or $1.03 per share in 1979 from $3,408,442 or $.72 per share in 1978.

During 1979 there was a decrease in business in the fast food industry, especially in those fast food operations that are hamburger oriented, due to a number of factors, including substantial price increases in the products sold to the consumer and the high level of competition in the fast food industry in some areas of the United States. In addition, unprecedented bad weather in the Winter and Spring in certain areas in which there are relatively high concentrations of *Dairy Queen* and *Dairy Queen/Brazier* stores had an adverse affect on the sales of the *Dairy Queen* System. Despite these factors, many stores were able to achieve significant increases in sales.

We believe our success in minimizing the impact of these negative factors is due, in part, to the introduction to the System in the Spring of 1979 of the "6 to 1" program. During 1978 we decided to simplify the marketing of *Brazier* hamburgers by introducing three hamburgers: the Single (one-sixth pound), the Double (one-third pound) and the Triple (one-half pound). The title "6 to 1" is derived from the fact that each patty weighs one-sixth of a pound. This program has reinforced, in the consumer's mind, the fact that hamburgers are available within our System. The *More Burger Than Bun* theme, which was introduced with the "6 to 1" program, is achieving its desired results.

As we reported last year, the *ICAN* program was introduced in November, 1978 in an effort to upgrade the appearance of *Dairy Queen* stores and the delivery of a high quality product to the consumer. While participation in this program has, to date, been adversely affected by high interest rates, a number of franchisees have elected to participate in the program. Improvements to these franchisees' stores include modernizations, conversions to full *Brazier*, conversions to limited *Brazier* and additions of drive-thru windows and dining rooms. These improvements appear to have contributed to a significant increase in the sales of many of such stores.

The Company is continuing various consumer awareness studies in order to better understand the consumers' perceptions of the *Dairy Queen* System and its products so that the Company and its franchisees can better serve the consumer and improve the operations of franchisees. Based on these studies, the Company has recently introduced a new marketing theme, *Its A Real Treat*, emphasizing product eye appeal in an effort to increase sales of *Dairy Queen* soft serve products

In conclusion, we want to acknowledge the significant contribution of our employees in helping to make 1979 another good year for your Company. Despite the major uncertainties and problems facing our country's economy as we enter the 1980's, we look forward to continued, consistent growth in this and future years.

Sincerely,

Harris Cooper

HARRIS COOPER
President

John W Mooty

JOHN W. MOOTY
Chairman of the Board

MANAGEMENT'S DISCUSSION AND ANALYSIS OF THE FINANCIAL SUMMARY

The improvement in the Company's net income in 1979 was due to a number of factors. There was an increase of $4,012,129 or 5.7% in revenues while expenses (before income taxes) increased,$2,502,671 or 3.9%. The following is a discussion of the reasons for the change from 1978 to 1979 and 1977 to 1978 in certain of the items of revenues and costs and expenses for such periods.

REVENUES (000s omitted)

	1979	1978	1977
	$74,871	$70,859	$63,432
Change	**+4,012**	+7,427	
Percent	**5.7%**	11.7%	

1979 Versus 1978:

Principal components of the increase from 1978 to 1979 are as follows:

Net Sales:	
Food and Supplies	+$2,825
Equipment	+ 316
Other	− 739
Service Fees	+ 1,408
Other	19

The increases in food and supplies and equipment resulted primarily from higher prices due to the continued increase in inflation and, to a lesser extent, increases in the number of units sold.

The decrease in net sales — other resulted from the discontinuance, late in 1978, of the Company's corporate store test program in San Diego, California.

The increase in service fees (revenues received from stores franchised by the Company and in connection with certain stores sub-franchised by territorial operators) was due to a number of factors which included increased prices charged for products sold by the stores due to inflation and the acquisition in 1978 and 1979 of the franchise rights of certain territorial operators. These increases were partially offset by a reduction in unit sales at the store level.

The increase in other was due to increases in interest income on notes and accounts receivable and short-term investments which were offset by a reduction in financing income due to a decrease in the number of equipment finance contracts entered into and the amortization of previous contracts plus a decrease in supplemental insurance commissions due to unfavorable claim experience.

1978 Versus 1977:

Principal components of the increase from 1977 to 1978 are as follows:

Net Sales.	
Food and Supplies	+$3,010
Equipment	+ 1,313
Mix	+ 596
Other	+ 687
Service Fees	+ 1,159
Franchise Sales and Other Fees	+ 321
Other	+ 278

The increase in food and supplies, equipment and mix resulted primarily from increases in the number of units sold and, to a lesser extent, higher prices due to inflation.

The increase in net sales — other resulted primarily from the inclusion of sales of the Company operated stores at the new Minnesota Zoological Garden which opened on May 22, 1978.

The increase in service fees resulted primarily from increased unit sales by stores and, to a lesser extent, increased prices charged for products sold by stores due to inflation.

The increase in franchise sales and other fees resulted from increased fees received from authorized warehouses and approved mix manufacturers due to their greater sales and increases in store transfer and training fees.

The increase in other revenues resulted from an increase in interest income on notes and accounts receivable and short-term investments and an increase in supplemental insurance commissions due to favorable claim experience. These increases were partially offset by a reduction in financing income due to a decrease in the number of equipment finance contracts entered into and the amortization of previous contracts.

COSTS AND EXPENSES (000s omitted)

	1979	1978	1977
	$66,783	$64,281	$59,287
Change	**+2,502**	+4,994	
Percent	**+3.9%**	+8.4%	

1979 Versus 1978:

Principal components of the increase from 1978 to 1979 are as follows:

Cost of Sales	+$1,560
Selling General & Administrative	+ 735
Interest	+ 177

The increase in cost of sales resulted primarily from higher costs due to the continued increase in inflation and, to a lesser extent, an increase in the number of units purchased. The percentage of cost of sales to net sales was 89.2% in 1979 and 90.0% in 1978.

The increase in selling, general and administrative expenses resulted primarily from the effect of inflation on employee compensation, travel expenses, vehicle operating costs and other miscellaneous operating expenses; a charge in connection with the election by certain employees to surrender their stock options in consideration for a cash payment equal to the difference between the market value of the common stock subject to their options and the exercise price of such options; and increased expenses for consumer awareness studies which were begun in 1978. These increases were partially offset by the continuation of the decrease in expenses relating to financial assistance provided certain franchisees due to the termination of franchises and the closing of stores in 1979 and prior periods.

The increase in interest expense resulted primarily from an increase in the interest rate on outstanding indebtedness. This increase was partially offset by a decrease in the average amount of outstanding indebtedness.

1978 Versus 1977:

Principal components of the increase from 1977 to 1978 are as follows:

Cost of Sales	+$4,747
Interest	+ 162

The increase in cost of sales resulted primarily from increases in the number of units purchased and, to a lesser extent, higher costs due to inflation. The percentage of cost of sales to net sales was 90.0% in 1978 and 90.7% in 1977.

The increase in interest expense resulted primarily from an increase in the interest rate on outstanding indebtedness. This increase was partially offset by a decrease in the average amount of outstanding indebtedness.

INCOME TAXES

The provision for income taxes as a percentage of income before income taxes was 48.5% in 1979, 48.2% in 1978, and 44.1% in 1977. The increases in the effective income tax rates in 1979 and 1978 are primarily due to the Company's higher earnings, without corresponding increases in franchise amortization available for income tax purposes and increases in state income taxes. For further information regarding income taxes, see Note 4 of the consolidated financial statements.

NET INCOME PER COMMON SHARE

The increases in net income per share in 1979 and 1978 were primarily due to increases in the Company's net income during each of such years. In addition, net income per share in 1979 and, to a lesser extent, in 1978 increased due to a decrease in the average number of common and common equivalent shares outstanding as a result of purchases by the Company of its securities in the open market and in privately negotiated transactions. The following table shows for the years indicated the net income per share (i) as reported: (ii) assuming that there had been no decrease in the number of common and common equivalent shares during 1979 and 1978; and (iii) assuming that there had been no decrease in the number of common and common equivalent shares during 1979. For purposes of the following calculations, net income for 1979, 1978 and 1977 has not been adjusted to give effect to the increase/decrease in interest expense for such years which may have occurred had the changes in common and common equivalent shares occurred in accordance with the stated assumptions. For further information regarding earnings per common share, see Note 1 of the consolidated financial statements.

Net Income Per Common Share

Net income per common share, based on net income (as reported) divided by	Year Ended November 30 1979	1978	1977
(i) Average common and common equivalent shares (as reported)	**$1.03**	$ .72	$ .42
(ii) Common and common equivalent shares as at November 30, 1977	**$ .86**	$ .71	$ 48
(iii) Common and common equivalent shares as at November 30, 1978	**$ .93**	$ .76	—

CONSOLIDATED STATEMENT OF INCOME
Years ended November 30, 1979 and 1978

	1979	1978 (As restated)
Revenues:		
Net sales	$54,412,505	$52,189,724
Service fees	13,049,220	11,640,716
Franchise sales and other fees	2,920,260	2,739,029
Real estate finance and rental income	3,356,605	3,175,863
Other	1,132,492	1,113,621
	74,871,082	70,858,953
Costs and expenses:		
Cost of sales	48,549,390	46,989,060
Expenses applicable to real estate finance and rental income	2,777,118	2,746,434
Selling, general and administrative	13,406,579	12,671,768
Interest	2,050,095	1,873,249
	66,783,182	64,280,511
Income before income taxes	8,087,900	6,578,442
Income taxes (Note 4)	3,920,000	3,170,000
Net income	$ 4,167,900	$ 3,408,442
Earnings per common share (Note 1)	$1.03	$ .72

See accompanying notes.

CONSOLIDATED BALANCE SHEETS
November 30, 1979 and 1978

ASSETS	1979	1978 (As restated)
Current assets:		
Cash	**$ 2,449,426**	$ 2,556,601
Commercial notes, at cost (approximates market)	**1,200,000**	4,600,000
Notes receivable, less allowance of $102,212 for doubtful notes (1978 — $148,043)	**576,119**	909,578
Accounts receivable, less allowance of $492,207 for doubtful accounts (1978 — $575,361)	**8,263,232**	7,018,759
Net investment in leases (Note 6)	**561,773**	571,521
Inventories	**1,359,268**	1,436,966
Deferred income taxes	**70,000**	105,000
Prepaid expenses	**537,760**	509,924
Total current assets	**15,017,578**	17,708,349
Other assets:		
Notes receivable, less allowance of $144,089 for doubtful notes (1978 — $112,148)	**1,599,324**	1,569,514
Miscellaneous (Note 1)	**2,019,045**	2,280,549
Total other assets	**3,618,369**	3,850,063
Other revenue producing assets:		
Net investment in leases (Note 6)	**4,779,256**	5,260,037
Rental properties, less accumulated depreciation of $2,177,912 (1978 — $2,550,137) (Notes 3 and 5)	**4,719,902**	4,219,203
Franchise rights and service contracts, at cost less accumulated amortization of $1,037,531 (1978 — $838,546) (Note 5)	**20,840,135**	19,477,531
Total other revenue producing assets	**30,339,293**	28,956,771
Property, plant and equipment, less accumulated depreciation of $1,554,548 (1978 — $1,323,676) (Note 3)	**2,113,091**	2,624,634
	$51,088,331	$53,139,817

See accompanying notes.

LIABILITIES AND STOCKHOLDERS' EQUITY	1979	1978 (As restated)
Current liabilities:		
10% note payable	$ —	$ 1,523,728
Drafts and accounts payable	**5,242,177**	5,318,397
Committed advertising	**2,854,214**	3,243,865
Other liabilities	**1,632,596**	1,769,665
Income taxes payable (Note 4)	**1,443,614**	1,770,121
Current maturities of long-term debt	**1,228,488**	975,419
Total current liabilities	**12,401,089**	14,601,195
Deferred franchise fees	**196,437**	161,283
Deferred income taxes	**275,000**	140,000
Long-term debt (Note 5)	**24,895,133**	25,666,257
Contingency and commitments (Notes 4, 6, and 9)		
Redeemable preferred stock (Notes 8 and 10):		
Special 7% cumulative preferred stock, Series B; 60,000 shares authorized, 39,942 shares issued and outstanding	**399,420**	399,420
Non-redeemable preferred stock, common stock and other stockholders' equity (Notes 10 and 11):		
Special 4% cumulative preferred stock, Series A; 450,000 shares authorized, 72,874 shares issued, including 6,733 treasury shares (1978 — 2,852)	**728,740**	728,740
Common stock, $1 par value; 10,000,000 shares authorized, 5,145,318 shares issued, including 2,314,403 treasury shares (1978 — 1,899,819)	**5,145,318**	5,145,318
Paid-in capital	—	195,730
Retained earnings (Notes 2 and 5)	**15,930,780**	11,860,259
	21,804,838	17,930,047
Less cost of treasury shares	**8,883,586**	5,758,385
Total non-redeemable preferred stock, common stock and other stockholders' equity	**12,921,252**	12,171,662
	$51,088,331	$53,139,817

See accompanying notes.

CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION
Years ended November 30,1979 and 1978

	1979	1978 (As restated)
Source of working capital:		
Operations:		
Net income	$ 4,167,900	$ 3,408,442
Items not involving working capital:		
Depreciation	679,728	747,032
Amortization	671,166	636,994
Deferred income taxes	135,000	125,000
Loss on disposal of property and equipment	285,019	185,742
Equity in foreign joint venture	(1,512)	(126,738)
Deferred franchise fees	(208,499)	(171,500)
Total from operations	5,728,802	4,804,972
Additions to long-term debt	1,826,627	7,013,645
Reduction of net investment in leases	740,143	880,204
Transfer of net investment in leases to rental properties	241,164	259,320
Proceeds of property and equipment disposals	1,124,264	1,189,262
Reduction in miscellaneous other assets	59,274	—
Decrease in notes receivable due after one year	—	391,910
Conversion of subordinated convertible debentures and exercise of stock options	639,714	349,016
	10,359,988	14,888,329
Disposition of working capital:		
Reduction in long-term debt	2,597,751	11,814,065
Transfer of net investment in leases to rental properties	241,164	259,320
Purchase of treasury shares	4,002,056	2,144,870
Additions to:		
Net investment in leases	500,526	110,561
Miscellaneous other assets	—	1,069,541
Rental properties	1,407,001	72,793
Franchise rights and service contracts	1,596,590	2,402,930
Property, plant and equipment	430,002	1,173,687
Deferred costs relating to deferred franchise fees	17,202	344,830
Dividends paid on special preference stock	55,968	56,288
Other	2,393	—
	10,850,653	19,448,885
Decrease in working capital (Note 7)	$ 490,665	$ 4,560,556

See accompanying notes.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
November 30, 1979 and 1978

1. Summary of significant accounting policies

Consolidation policy and basis of presentation —

The consolidated financial statements include the accounts of the Company and its subsidiaries, all of which are wholly-owned. All significant intercompany transactions are eliminated in consolidation. Gains from translation of financial statements of Canadian subsidiaries were approximately $80,000 and $150,000 in 1979 and 1978, respectively.

Certain reclassifications have been made in the 1978 financial statements to make them comparable with the presentations for 1979.

Segment information —

The Company operates in one industry segment: developing, licensing, franchising and servicing a system of retail stores featuring over-the-counter sales of food and dairy desserts.

Franchise sales and service fees —

The Company recognizes revenues from initial store franchise fees when the store is opened. Direct costs incurred prior to store openings are deferred until the revenue is recognized. Continuing franchise service fees are recognized as earned.

Inventories —

Inventories consist primarily of store equipment and merchandise and are carried at the lower of cost (first-in, first-out) or market (primarily net realizable value).

Depreciation and amortization —

Depreciation and amortization of rental properties and property, plant and equipment are provided principally on the straight-line method over estimated useful lives of 15 to 40 years for buildings, 5 to 10 years for equipment and over the shorter of the useful life of the asset or the remaining term of the lease for leasehold improvements.

The Company believes there has been no diminution in the value of franchise rights and service contracts since the dates of their acquisition and follows a policy of non-amortization of franchise rights and service contracts acquired prior to November 1970. The cost of franchise rights and service contracts acquired subsequent to October 31, 1970 (approximately $8,900,000) is being amortized over 40 years.

Debt issue costs are amortized on the debt-outstanding method. Unamortized costs of $1,267,586 and $1,429,175 at November 30, 1979 and 1978, respectively, are included with "miscellaneous other assets" in the consolidated balance sheet.

Repairs and maintenance —

Repairs and maintenance are charged to expense as incurred. The costs of renewals and betterments are capitalized. When properties are retired or otherwise disposed of, the costs and the related accumulated depreciation or amortization are removed from the accounts. Gains or losses from disposals are included in operations.

Committed advertising —

Committed advertising represents unexpended amounts received from franchisees to finance national and regional advertising programs.

Income taxes —

Investment tax credits are accounted for on the flow-through method.

The Company has not provided for income taxes on the undistributed earnings of its Canadian subsidiaries ($2,654,163 as of November 30, 1979) as, to the extent these earnings may be repatriated in the near future, foreign tax credits will be available to substantially eliminate any income taxes which might otherwise result from such repatriation.

Earnings per common share —

Earnings per common share amounts are based on the weighted average number of common and dilutive common equivalent shares outstanding during each year (4,134,882 in 1979 and 4,852,906 in 1978). Dilutive common share equivalents consist of shares issuable upon (a) conversion of subordinated convertible debentures, (b) exercise of stock options (after reduction for common shares assumed to have been purchased with the proceeds) and (c) conversion of Series A and Series B special preference stock. For purposes of the computations, net income has been increased by interest costs, net of income taxes, on the subordinated convertible debentures. Fully-diluted earnings per common share do not differ materially from primary earnings per common share. If the common shares purchased for the treasury in 1978 and 1979 had been purchased as of December 1, 1977, earnings per share for 1979 and 1978, without giving effect to interest costs on funds used to purchase these shares, would have been $1.07 and $.81, respectively.

2. Restatement of prior year's financial statements

The financial statements for the year ended November 30, 1978, and retained earnings as of November 30, 1977, have been restated to give retroactive effect to Statement No. 13 of the Financial Accounting Standards Board, Accounting For Leases. The effect of this accounting change was to decrease retained earnings as of November 30, 1977 by $303,817 and to increase net income for the year ended November 30, 1978 by $56,024 ($.01 per share). The Company's leasing transactions are described in Note 6.

3. Rental properties and property, plant and equipment

Rental properties and property, plant and equipment consist of:

	1979	1978
Rental properties, at cost:		
Land	**$2,274,221**	$1,120,166
Buildings	**4,089,458**	4,874,174
Equipment	**286,705**	440,561
Leasehold improvements	**247,430**	334,439
	6,897,814	6,769,340
Less accumulated depreciation	**2,177,912**	2,550,137
	$4,719,902	$4,219,203

Property, plant and equipment, at cost:		
Land	**$ 97,383**	$ 298,209
Buildings	**600,002**	1,017,149
Equipment	**1,944,681**	1,671,010
Leasehold improvements	**1,025,573**	961,942
	3,667,639	3,948,310
Less accumulated depreciation	**1,554,548**	1,323,676
	$2,113,091	$2,624,634

4. Income taxes

Income taxes consist of the following:

	1979	1978
Current:		
Federal	**$2,685,000**	$2,290,000
State	**345,000**	235,000
Foreign	**720,000**	505,000
	3,750,000	3,030,000
Deferred:		
Federal	**140,000**	130,000
State	**15,000**	5,000
Foreign	**15,000**	5,000
	170,000	140,000
	$3,920,000	$3,170,000

The provision for federal income taxes has been reduced by investment tax credits of approximately $20,000 in 1979 and increased by the recapture of investment tax credits of approximately $30,000 in 1978.

The following is a reconciliation of differences between the federal statutory income tax rate and the consolidated effective tax rate:

	1979	1978
Federal statutory rate	**46.2%**	48.0%
Amortization of franchise rights for income tax purposes which are not being amortized for financial accounting purposes	**(.5)**	(1.9)
State income taxes, net of federal effect	**2.4**	1.9
Other, net	**.4**	.2
Consolidated effective tax rate	**48.5%**	48.2%

Deferred income taxes relate to the differences between taxable income and income reported for financial statement purposes and consist of the following:

	1979	1978
Leases reported on the operating method for income tax purposes	**$ 26,000**	$ (33,000)
Accelerated tax depreciation	**6,000**	8,000
Provision for expenses and losses deductible in different periods for income tax purposes	**107,000**	57,500
Amortization of franchise rights over different periods for tax and book purposes	**67,000**	27,000
Other items (not in excess of 5%)	**(36,000)**	80,500
	$170,000	$140,000

The Internal Revenue Service has examined the Company's income tax returns for 1973 through 1975 and is examining the income tax returns for years 1976 through 1978. In connection with the examination of 1973 through 1975 income tax returns, certain adjustments were proposed by the Internal Revenue Service which would not materially affect the financial position or operating results of the Company.

Also, in connection with the examination of the 1973 through 1975 income tax returns, the Internal Revenue Service has taken the position that funds received by the Company from its franchisees in connection with the sales promotion programs and not reported as income are taxable to the Company. Further, the Internal Revenue Service has also proposed to create a new taxpayer, which it labels "IDQ Advertising Fund," as a vehicle for the taxation of the same sales promotion funds. The Company and its legal counsel believe that the creation of a new taxpayer will not be sustained, and that the Company's position against the taxation to the Company of the sales promotion program funds is meritorious and should prevail.

5. Long-term debt

Long-term debt is summarized as follows:

	1979	1978
Subordinated convertible debentures, bearing interest at ½% over prime rate (16¼% at November 30, 1979), maturing in 1981	**$ 1,242,431**	$ 1,670,657
10¼% subordinated capital notes, maturing in 1986	**3,000,000**	3,000,000
10% subordinated capital notes, maturing in 1987	**4,980,000**	4,990,000
10% subordinated capital notes, maturing in 1988	**6,924,000**	7,000,000
6% to 11% notes payable, secured by franchise rights and service contracts, maturing at various dates through 1997 (current maturities — $380,022 in 1979 and $268,852 in 1978)	**3,110,354**	2,413,214
6% to 11½% real estate mortgages and contracts payable, maturing at various dates through 1995 (current maturities — $217,375 in 1979 and $50,914 in 1978)	**677,464**	349,694
Obligations under capital leases (current maturities — $621,739 in 1979 and $628,310 in 1978) (Note 6)	**6,167,673**	7,158,986
Other long-term debt (current maturities — $9,352 in 1979 and $27,343 in 1978)	**21,699**	59,125
	26,123,621	26,641,676
Less current maturities	**1,228,488**	975,419
	$24,895,133	$25,666,257

The subordinated convertible debentures are convertible at the option of the holders into shares of common stock at the rate of $1.50 per share at any time prior to maturity.

The capital notes are subordinated to bank and approximately $295,000 of other indebtedness. The capital notes issued in 1976 and 1977 were issued under indentures which provide that the notes are subject to redemption by the Company after their first year at a 5% premium, which is reduced 1% annually through the sixth year, after which they are redeemable at par. The capital notes issued in 1978 were issued under an indenture which provides for redemption by the Company after the first year at a 5% premium, which is reduced approximately .6% annually through the ninth year, after which they are redeemable at par.

The Company has a revolving credit agreement which provides for borrowings up to $10,000,000 through September 1, 1981, and the due date may be extended from time to time by mutual consent of the Company and the banks. The agreement provides for interest at ¼% in excess of the prime interest rate on the outstanding balance and for a commitment fee of ½% of the unused credit. The loans are secured by the outstanding stock of the Company's subsidiaries. In connection with the revolving credit agreement, the Company has informally agreed to maintain an average annual compensating balance, not restricted as to withdrawal, of an amount equal to the sum of 5% of the line of credit and 15% of the usage under such line. The average compensating balances amounted to approximately $830,000 in 1979 and $1,260,000 in 1978. There were no borrowings under this line of credit at November 30, 1978 or 1979.

The Company's revolving credit agreement and the capital note indentures contain provisions which, among other things, limit additional indebtedness and commitments under lease agreements and limit the amount available for dividends and redemption or purchase of the Company's capital stock. At November 30, 1979 approximately $765,000 would be available for payment of dividends and redemption or purchase of capital stock.

Franchise rights of $5,380,000, rental properties of $490,000, and notes receivable of $180,000 are pledged to secure certain long-term debt.

Other than obligations under capitalized leases, aggregate maturities of long-term debt for years subsequent to November 30, 1980 are: $1,758,000, $453,000, $453,000, $561,000, and $16,124,000 in 1981, 1982, 1983, 1984, and thereafter, respectively. For maturities of capitalized lease obligations, see Note 6.

6. Leases

The Company and its subsidiaries have leases for *Dairy Queen* retail stores, and administrative facilities and equipment. Certain of the leased properties are subleased to franchise operators under noncancellable subleases with rentals generally equal to or greater than rentals payable on the prime leases. Most of the leases and subleases require the lessee to pay executory costs (property taxes, maintenance and insurance); and many of the leases provide for one or more renewal options. In addition, Company-owned real estate has been leased to franchise operators under long-term leases.

Net investment in leases —

	Building and equipment		
	Owned	Leased	Total
	(000s omitted)		
1979			
Minimum future rents, including residual values	$2,027	$6,792	$8,819
Less unearned income	828	2,650	3,478
Net investment	1,199	4,142	5,341
Less current portion	201	361	562
Non-current net investment	$ 998	$3,781	$4,779
1978			
Minimum future rents, including residual values	$2,579	$7,167	$9,746
Less unearned income	1,057	2,857	3,914
Net investment	1,522	4,310	5,832
Less current portion	227	345	572
Non-current net investment	$1,295	$3,965	$5,260

Minimum future lease rentals receivable under leases of owned properties at November 30, 1979 are $326,000, $255,000, $188,000, $144,000, $123,000, and $991,000 in 1980, 1981, 1982, 1983, 1984, and 1985-1997, respectively. Minimum future lease rentals under leases of subleased properties at November 30, 1979 are $800,000, $785,000, $761,000, $732,000, $693,000, and $3,021,000 in 1980, 1981, 1982, 1983, 1984, and 1985-1997, respectively.

Obligations under capitalized leases —

	1979	1978
	(000s omitted)	
Minimum future obligations	**$ 9,668**	$11,580
Less amount representing interest	**3,500**	4,421
Present value of net minimum obligation	**6,168**	7,159
Less current portion	**622**	628
Non-current obligations	**$ 5,546**	$ 6,531

Minimum future obligations, including interest, for years subsequent to November 30, 1979, are $1,244,000, $1,228,000, $1,109,000, $1,062,000, $989,000, and $4,036,000 in 1980, 1981, 1982, 1983, 1984, and 1985-1997, respectively.

Equipment under capitalized leases in the amount of $355,550 at November 30, 1979 and November 30, 1978 is included in property, plant and equipment in the accompanying balance sheet. Buildings under capital leases in the amount of $3,024,805 at November 30, 1979 and $4,058,759 at November 30, 1978 are included in rental properties in the accompanying balance sheet. Accumulated depreciation at November 30, 1979 and November 30, 1978 on equipment and buildings capitalized under these lease agreements was $1,763,566 and $2,161,581, respectively.

Operating leases —

Total rental expenses in the statement of income, including rentals on leases with terms of one year or less and including executory costs when included in rent, are summarized as follows:

	1979	1978
Minimum rentals	**$2,643,558**	$2,577,899
Contingent rentals	**131,986**	131,429
Less sublease income —		
Minimum rentals	**(2,193,042)**	(2,100,265)
Contingent rentals	**(361,555)**	(243,759)
	$ 220,947	$ 365,304

Minimum future rental obligations, excluding executory costs included in rentals, under operating leases at November 30, 1979 are $1,786,000, $1,646,000, $1,521,000, $1,376,000, $1,238,000, and $4,203,000 in 1980, 1981, 1982, 1983, 1984, and 1985-1997, respectively.

Minimum future lease rentals receivable under operating leases at November 30, 1979 are $1,655,000, $1,469,000, $1,353,000, $1,194,000, $1,036,000, and $4,265,000 in 1980, 1981, 1982, 1983, 1984, and 1985-1997, respectively.

7. Working capital

	1979	1978
Analysis of (increase) decrease in working capital:		
Cash	**$ 107,175**	$7,448,593
Commercial notes	**3,400,000**	(4,600,000)
Receivables	**(911,014)**	(955,733)
Net investment in leases	**9,748**	30,484
Inventories	**77,698**	295,100
Deferred income taxes	**35,000**	15,000
Prepaid expenses	**(27,836)**	(15,030)
Note payable	**(1,523,728)**	1,523,728
Drafts and accounts payable	**(76,220)**	684,619
Committed advertising	**(389,651)**	737,441
Other liabilities	**(137,069)**	612,960
Income taxes payable	**(326,507)**	(454,379)
Current maturities of long-term debt	**253,069**	(762,227)
Decrease in working capital	**$ 490,665**	$4,560,556

8. Redeemable preferred stock

The outstanding Series B stock is redeemable, with certain exceptions, at the option of the Company or the holder at par value plus accrued dividends. The Company may redeem each year up to 25% of the shares outstanding at the previous year end. The holder is limited during the first five years after issuance to redeeming, on a cumulative basis, a maximum of 10% of the original number of shares. Assuming maximum shareholder redemption, redemption requirements for years subsequent to November 30, 1979 are $136,900, $62,790, $57,080, and $142,650 in 1980, 1981, 1982, and 1983, respectively.

9. Commitment

During January 1980, the Company purchased 28,037 shares of its 4% Series A preferred stock and 51,963 shares of its common stock for an aggregate purchase price of $480,000, and agreed to purchase, on or before August 31, 1980, 156,879 shares of its common stock at a purchase price of $980,494. The Company's obligation to purchase the 156,879 common shares is subject to its ability to effect such purchase without violating certain restrictions regarding the purchase of the Company's common stock contained in indentures pursuant to which the Company's capital notes were issued

10. Non-redeemable preferred stock, common stock and other stockholders' equity

The presentation in the balance sheet for accounts previously classified as stockholders' equity has been revised in the accompanying balance sheet to reflect a requirement of the Securities and Exchange Commission which became effective in 1979. The revised presentation requires that the Company's redeemable preferred stock be presented separately in the balance sheet from the other accounts referred to above. See Note 8.

There were no changes in the issued non-redeemable special 4% cumulative preferred stock, Series A, or in issued common stock in 1978 or 1979.

Changes in other stockholders' equity is shown below:

	Paid-in capital	Retained earnings	Treasury shares
Balance at November 30, 1977, as previously reported	$ 404,728	$ 8,811,922	$ 4,171,529
Restatement for change in accounting method for leases (Note 2)		(303,817)	
Balance at November 30, 1977, as restated	404,728	8,508,105	4,171,529
Net income		3,408,442	
Dividends paid on preferred stocks		(56,288)	
Issue of 209,560 shares of common treasury stock upon conversion of subordinated debentures	(204,626)		(518,966)
Issue of 14,500 shares of common treasury stock upon exercise of stock options	(4,372)		(39,048)
Purchase of 447,659 shares of common stock and 800 Series A preferred shares for the treasury			2,144,870
Balance at November 30, 1978	195,730	11,860,259	5,758,385
Net income		4,167,900	
Dividends paid on preferred stock		(55,968)	
Issue of 285,480 shares of common treasury stock upon converson of subordinated debentures	(197,222)	(41,411)	(667,182)
Issue of 84,175 shares of common treasury stock upon exercise of stock options	1,492		(209,673)
Purchase of 784,239 shares of common stock and 3,881 Series A preferred shares for the treasury			4,002,056
Balance at November 30, 1979	$ —	$15,930,780	$ 8,883,586

The Company's Board of Directors is authorized to issue 1,000,000 shares of special preference stock, par value $10.00, in one or more series and to determine voting rights, dividend rates, redemption rights, convertibility and other preferences of each series. The Board of Directors has authorized two series of special preference stock designated as Series A and Series B. Each share of outstanding Series A and Series B stock is convertible, at the option of the holder, into one share of common stock. The outstanding Series A stock is redeemable, at the Company's option, at par value plus accrued dividends. For a description of Series B stock, see Note 8.

Shares of common stock held in treasury at November 30, 1979 were reserved for issuance as follows:

Conversion of subordinated debentures convertible at $1.50 per share	828,287
Conversion of special preference stock convertible at $10.00 per share	106,083
Exercise of stock options	218,375
	1,152,745

11. Stock options

The Company's qualified stock option plan provides for the granting of options for up to 300,000 shares of common stock to certain officers and key employees at not less than 100% of fair market value. In addition, as of November 30, 1979, the Company has granted nonqualified options to officers for a total of 56,000 shares at not less than 100% of fair market value. All options are exercisable at any time, in whole or in part, and expire five years after the date of grant. In 1979 and 1978, \$384,701 and \$37,500, respectively, was charged to operations as compensation, as the result of the surrender or exercise of certain options for cash. Upon exercise of stock options, proceeds received in excess of par value of the common stock are credited to paid-in capital.

During fiscal 1973, options for 142,300 shares ("replacement options") at \$6.25 per share were granted to employees holding qualified options for an equivalent number of shares at prices ranging from \$8.25 to \$20.00 and granted at various dates from 1971 to 1973. During fiscal 1976, replacement options at \$2.50 per share were granted to employees holding 1973 replacement options for an equivalent number of shares at \$6.25. The replacement options expire five years from date of grant, may not be exercised while the prior option or prior replacement option is outstanding, and terminate in the event of the exercise of the prior option or prior replacement option.

Changes in options outstanding during 1978 and 1979 are summarized as follows:

	Number of shares	Option price Per share	Option price Total	Market value Per share	Market value Total
Options outstanding November 30, 1977	231,125	$1.75-9.75	$ 774,840	$1.75-9.75	$774,840(A)
Cancelled in 1978	(5,625)	2.13-6.25	(19,880)		
Surrendered in 1978	(15,000)	1.75	(26,250)		
Exercised in 1978	(14,500)	2.00-2.50	(34,676)	4.50-6.50	81,825(B)
Granted in 1978	19,500	2.15-3.35	53,515	2.15-3.35	53,515(A)
Replacement option effect	—		(245,000)		
Options outstanding November 30, 1978	215,500	1.75-3.63	502,549	1.75-3.63	502,549(A)
Cancelled in 1979	(4,875)	2.15-2.38	(10,704)		
Surrendered in 1979	(34,625)	1.75-2.88	(83,941)		
Exercised in 1979	(84,175)	2.00-3.63	(211,165)	4.38-6.25	501,423(B)
Options outstanding November 30, 1979	91,825	1.75-2.88	$ 196,739	1.75-2.88	196,739(A)
Options becoming exercisable:					
1978	21,750	2.00-3.63	$ 48,216	3.13-5.63	91,136(C)
1979	65,750	2.00-3.35	157,948	4.13-6.25	395,594(C)

(A) At dates options were granted.
(B) At dates options were exercised.
(C) At dates options became exercisable.

At November 30, 1979, options for 91,825 shares were exercisable (1978 — 149,750 shares) and 126,550 shares (1978 — 126,550 shares) were available for future grant under the qualified plan.

12. Quarterly financial data

Quarterly operating data (unaudited) for fiscal 1979 and 1978 is as follows (000s omitted, except per share amounts):

	1979 First quarter	1979 Second quarter	1979 Third quarter	1979 Fourth quarter	1978 First quarter	1978 Second quarter	1978 Third quarter	1978 Fourth quarter
Net sales	$ 8,718	$17,441	$18,122	$10,132	$ 6,741	$15,958	$18,475	$11,016
Cost of sales	7,770	15,520	16,173	9,086	6,112	14,291	16,481	10,105
	948	1,921	1,949	1,046	629	1,667	1,994	911
Service fees and other revenues	3,275	5,678	7,044	4,461	2,651	5,049	6,600	4,369
	4,223	7,599	8,993	5,507	3,280	6,716	8,594	5,280
Other costs and expenses	4,508	4,427	4,526	4,773	4,126	3,977	4,347	4,842
Income (loss) before taxes	(285)	3,172	4,467	734	(846)	2,739	4,247	438
Income taxes	(138)	1,538	2,167	353	(408)	1,320	2,047	211
Net income (loss)	$(147)	$ 1,634	$ 2,300	$ 381	$(438)	$ 1,419	$ 2,200	$ 227
Earnings per share	$(.05)	$ .39	$ .57	$ .10	$(.13)	$ .29	$ .46	$ .05

The above amounts have been restated to give effect to Statement of Financial Accounting Standards No. 13, Accounting for Leases, referred to in Note 2, which was adopted in the fourth quarter of 1979. The increase/(decrease) in previously reported net income for the quarters ended March 2, June 1, and August 31, 1979 was \$742, \$48,612, and \$(8,743), respectively. The increase/(decrease) in previously reported net income for the quarters ended February 24, May 26, August 25, and November 30, 1978 was \$9,639, \$7,343, \$(5,307), and \$44,349, respectively. Quarterly earnings per share have not been affected significantly by the restatement.

REPORT OF CERTIFIED PUBLIC ACCOUNTANTS

The Board of Directors and Stockholders
International Dairy Queen, Inc.

We have examined the accompanying consolidated balance sheets of International Dairy Queen, Inc. at November 30, 1979 and 1978, and the related consolidated statements of income and changes in financial position for the years then ended. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the statements mentioned above present fairly the consolidated financial position of International Dairy Queen, Inc. at November 30, 1979 and 1978, and the consolidated results of operations and changes in financial position for the years then ended, in conformity with generally accepted accounting principles applied on a consistent basis during the period, after restatement of the financial statements for 1978 to give retroactive effect to the change, with which we concur, in the method of accounting for leases as described in Note 2 to the financial statements.

Minneapolis, Minnesota
January 19, 1980

ARTHUR YOUNG & COMPANY

INTERNATIONAL DAIRY QUEEN, INC.

CORPORATE DIRECTORY

BOARD OF DIRECTORS

*HARRIS COOPER	*President and Chief Executive and Chief Operating Officer of the Company*
JAMES C. CRUIKSHANK	*Private Investor*
ERNEST F. DORN	*Chairman of the Board of Directors of Community Credit Company*
*RUDY LUTHER	*President of Hansord Pontiac Company*
RAYMOND MITHUN	*Chairman of Mithun Enterprises, Inc., a holding company; Chairman of Executive Committee of Campbell-Mithun, Inc., an advertising agency*
*FRANK O. MOFFETT	*Private Investor*
JANE N. MOOTY	*Private Investor*
*JOHN W. MOOTY	*Chairman of the Board and Chairman of the Executive Committee; Partner in the Minneapolis law firm of Gray, Plant, Mooty, Mooty & Bennett*
RAYMOND C. SCHWEIGERT	*Consultant and General Manager of Schweigert Meat Company*

*Members of the Executive Committee

OFFICERS

JOHN W. MOOTY	*Chairman of the Board and Chairman of the Executive Committee*
HARRIS COOPER	*President and Chief Executive and Chief Operating Officer*
GORDON F. HUBER	*Executive Vice President*
GLENN H. MUEFFELMANN	*Executive Vice President*
FRANK L. HEIT	*Executive Vice President and Treasurer*
DAVID M. BOND	*Controller and Assistant Treasurer*
MARK S. BROIN	*Vice President — Management Information Systems and Human Resources Development*
EDWARD P. GHERITY	*Vice President — Purchasing and Distribution*
MICHAEL J. LEARY	*Vice President — Canadian Operations and Institutional*
HERMAN E. NELSON	*Vice President — Law*
GARY H. SEE	*Vice President — Marketing*
GILBERT N. STEMMERMAN	*Vice President — Franchise Development/International Division*
MICHAEL P. SULLIVAN	*Secretary; Partner in the Minneapolis law firm of Gray, Plant, Mooty, Mooty & Bennett*
WALTER S. TELLEGEN	*Vice President — Franchise Operations*
WILLIAM R. VON HASSEL	*Vice President — Equipment*
EDWARD A. WATSON	*Vice President — Territory Operator/Supervised Store Division*

THE COMPANY
International Dairy Queen, Inc. is engaged in the business of developing, licensing, franchising and servicing a system of retail stores featuring hamburgers and various dairy desserts which are marketed under the *Brazier* and *Dairy Queen* trademarks. Since the opening of the first *Dairy Queen* store in 1940, the System has expanded on a national and international basis and at November 30, 1979 was comprised of 4,860 stores, of which 4,336 stores were located in the United States, 365 stores in Canada, and 159 stores in other countries. Of the 4,860 stores, 2,498 were franchised by the Company, 6 were operated by the Company, and 2,356 were subfranchised by licensed territorial operators.

ANNUAL MEETING
The annual meeting of shareholders will be held Wednesday, February 27, 1980 at 10:00 a.m. in the General Offices of the Company.

FORM 10-K
A copy of the Company's Annual Report on Form 10-K to the Securities and Exchange Commission, including the financial statements and schedules thereto, can be obtained by writing to the Company at the General Offices, Attention: Glenn H. Mueffelmann.

GENERAL OFFICES
International Dairy Queen, Inc.
5701 Green Valley Drive
Minneapolis, Minnesota 55437
(612) 830-0200

AUDITORS
Arthur Young & Company
Minneapolis, Minnesota 55402

COUNSEL
Gray, Plant, Mooty, Mooty & Bennett
Minneapolis, Minnesota 55402

REGISTRAR
Northwestern National Bank
of Minneapolis, 55480

TRANSFER AGENT
Northwestern National Bank
of Minneapolis, 55480

STOCK DATA
Traded on the National Over-the-Counter Market

NASDAQ SYMBOL:
INDQ

PRICE RANGE OF COMMON STOCK
The low and high bid and asked prices for the Company's common stock in the over-the-counter market for the periods shown, as reported by the National Association of Securities Dealers, Inc., are as indicated below. These prices do not include retail mark-up or commission, and do not necessarily reflect actual transactions.

	Bid		Asked	
PERIOD — FISCAL YEAR 1979	**Low**	**High**	**Low**	**High**
First Quarter	3½	5⅞	4⅛	6⅜
Second Quarter	4¾	5¾	5¼	6¼
Third Quarter	4⅞	5¾	5⅜	6¼
Fourth Quarter	4⅜	5¼	4⅞	5¾
PERIOD — FISCAL YEAR 1978				
First Quarter	2¼	3	2⅝	3⅜
Second Quarter	2⅞	5⅞	3⅛	6⅜
Third Quarter	4½	6⅜	5	6⅞
Fourth Quarter	3½	6	4	6½

Dividends have not been paid on common stock.